

**NEBRASKA LIFE AND HEALTH INSURANCE
GUARANTY ASSOCIATION**

Financial Statements

December 31, 2003 and 2002

and

Independent Auditor's Report

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Nebraska Life and Health
Insurance Guaranty Association

I have audited the accompanying statements of financial position of Nebraska Life and Health Insurance Guaranty Association as of December 31, 2003 and 2002, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Association's management. My responsibility is to express an opinion on these financial statements based on my audits.

I conducted my audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audits provide a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Nebraska Life and Health Insurance Guaranty Association as of December 31, 2003 and 2002, and the results of its activities and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Walter L. Waltke

Certified Public Accountant

February 12, 2004

STATEMENTS OF FINANCIAL POSITION (Notes 1 and 2)

| | Dec. 31, <u>2003</u> | Dec. 31, <u>2002</u> |
|---|-------------------------|-------------------------|
| ASSETS: | | |
| Cash in checking account | \$ 151,437 | \$ 244,592 |
| Cash in money market fund | 665,894 | 875,161 |
| U. S. Treasury Notes at market value (Note 3) | 3,142,500 | 3,187,190 |
| U. S. Government Agency bonds at market value (Note 4) | 4,867,783 | 4,843,791 |
| Corporate bonds at market value (Note 5) | 1,593,168 | 1,258,611 |
| Accrued interest receivable on investments | 80,795 | 90,808 |
| Equipment – Cost | 5,520 | 5,520 |
| – Accumulated depreciation | <u>(5,520)</u> | <u>(5,520)</u> |
| TOTAL ASSETS | <u>\$10,501,577</u> | <u>\$10,500,153</u> |
| LIABILITIES: | | |
| Accounts payable | \$ 994 | \$ 7,382 |
| Estimated claims payable (Note 6) | <u>6,337,748</u> | <u>4,540,000</u> |
| TOTAL LIABILITIES | <u>\$ 6,338,742</u> | <u>\$ 4,547,382</u> |
| NET ASSETS: | | |
| UNRESTRICTED NET ASSETS: | | |
| Class A net assets for general administration | \$ 191,544 | \$ 162,905 |
| Equipment net assets – Class A | <u>0</u> | <u>0</u> |
| Total Unrestricted Net Assets | <u>\$ 191,544</u> | <u>\$ 162,905</u> |
| TEMPORARILY RESTRICTED NET ASSETS: | | |
| Classes B and C net assets for specific insurance company insolvencies (Exhibit A-1) | \$ 1,532,564 | \$ 3,467,435 |
| Contingency reserve for future obligations (Note 7) | <u>2,438,727</u> | <u>2,322,431</u> |
| Total Temporarily Restricted Net Assets | <u>\$ 3,971,291</u> | <u>\$ 5,789,866</u> |
| TOTAL NET ASSETS | <u>\$ 4,162,835</u> | <u>\$ 5,952,771</u> |
| TOTAL LIABILITIES AND NET ASSETS | <u>\$10,501,577</u> | <u>\$10,500,153</u> |

See accompanying notes to financial statements.

CLASSES B AND C NET ASSETS FOR SPECIFIC INSURANCE COMPANY INSOLVENCIES

| | <u>12/31/03</u> | <u>12/31/02</u> |
|--|-----------------|-----------------|
| Class C 7 – First Columbia Life, Louisiana | \$ (11,948) | \$ (11,658) |
| Class C 9 – Amalgamated Labor Life, Illinois | 0 | 96,481 |
| Class C 11 – Knickerbocker Life, Texas | 57,261 | 55,871 |
| Class C 13 – Life of Indiana, Indiana | 27,829 | 27,153 |
| Class C 20 – Executive Life, California | (5,580,475) | (5,121,336) |
| Class C 21 – Mutual Security Life, Indiana | 5,795,962 | 5,655,310 |
| Class C 23 – First Capital Life, California and Fidelity Bankers Life, Virginia | 0 | 25,752 |
| Class C 25 – Midwest Life, Louisiana | 623,540 | 608,718 |
| Class C 26 – Guaranty Security Life, Florida | 2,235,836 | 1,957,828 |
| Class C 27 – Mutual Benefit Life, New Jersey | 271,436 | 259,981 |
| Class C 28 – United Equitable Life, Illinois | 0 | (39,103) |
| Class C 29 – Inter-American Insurance, Illinois | 604,351 | 566,698 |
| Class C 30 – Andrew Jackson Life, Mississippi | (2,034) | (1,985) |
| Class C 31 – Great Republic Life, California | (2,497) | (2,436) |
| Class C 32 – Old Faithful Life, Wyoming | 101,609 | 99,143 |
| Class C 33 – Old Colony Life, Georgia | 325,929 | 318,017 |
| Class C 34 – New Jersey Life, New Jersey | 55,385 | 54,041 |
| Class C 36 – Pacific Standard Life, California | (13) | 1,132 |
| Class C 37 – Kentucky Central Life, Kentucky | 886,255 | 865,717 |
| Class C 38 – Consumers United, Delaware | (146,499) | (142,808) |
| Class C 40 – American Integrity, Pennsylvania | 897,854 | 876,060 |
| Class C 41 – National Heritage Life, Delaware | (103,691) | (98,182) |
| Class C 42 – Summit National Life, Pennsylvania | 171,777 | 167,730 |
| Class C 43 – Confederation Life, Michigan | (6,852) | (7,225) |
| Class C 45 – National American Life, Pennsylvania | 147,786 | 144,232 |
| Class C 49 – First National Life, Alabama | (1,210) | (1,228) |
| Class C 52 – American Standard Life, Oklahoma | (84,314) | (80,391) |
| Class C 53 – Professional Benefits Insurance, Texas | (3,277) | (5,786) |
| Class C 54 – Centennial Life, Kansas | (86,202) | (90,604) |
| Class C 55 – Universe Life, Idaho | (289,450) | (281,508) |
| Class C 56 – Fidelity Bankers Life, Virginia | (497,657) | (485,553) |
| Class C 57 – Statesman National Life, Texas | (8,642) | (7,925) |
| Class C 58 – Settlers Life, Virginia | 0 | (1,645) |
| Class C 60 – First National Life Ins. Co. of America, MS (Thunor) | (316,932) | (307,945) |
| Class C 61 – International Financial Services Life, MO (Thunor) | (8,419) | (8,214) |
| Class C 62 – National Affiliated Investor Life, Louisiana | (17,570) | (16,709) |
| Class C 63 – American Chambers Life, Ohio | (1,405,084) | (1,368,799) |

(Continued)

CLASSES B AND C NET ASSETS FOR SPECIFIC INSURANCE COMPANY INSOLVENCIES

| (Continued) | <u>12/31/03</u> | <u>12/31/02</u> |
|---|---------------------|---------------------|
| Class C 64 – Bankers Commercial Life, Texas | \$ (31,327) | \$ (43,403) |
| Class C 65 – Reliance Insurance Co., Pennsylvania | (13,002) | (177,705) |
| Class B 66 – Legion & Villanova Insurance Cos., Pennsylvania | (5,413) | (2,798) |
| Class B 67 – London Pacific Life, North Carolina | <u>(2,047,738)</u> | <u>(7,483)</u> |
| Total Classes B and C Net Assets for Specific Insurance Company Insolvencies | \$ <u>1,532,564</u> | \$ <u>3,467,435</u> |

STATEMENTS OF ACTIVITIES (Notes 1 and 2)

| | Class A | Classes B & C (Exh. B-1) | Total 2003 | 2002 |
|--|------------|-----------------------------|---------------|-------------|
| REVENUES: | | | | |
| Estate distributions | | \$ 286,372 | \$ 286,372 | \$1,935,023 |
| Insurance premiums received | | 3,709 | 3,709 | 34,617 |
| Investment income – Net (Note 8) | \$ 4,532 | 252,403 | 256,935 | 613,819 |
| Refund overpayment of assessments | | | 0 | (17,920) |
| TOTAL REVENUES | \$ 4,532 | \$ 542,484 | \$ 547,016 | \$2,565,539 |
| EXPENSES: | | | | |
| Assumption reinsurance | | \$ 389,355 | \$ 389,355 | \$ 351,595 |
| Policyholder benefit claims | | (951) | (951) | 42,035 |
| Claims processing services | | | 0 | 169 |
| Assessments by NOLHGA for expenses | \$ 20,547 | 43,997 | 64,544 | 43,071 |
| Administration & legal fees, & direct expenses | 28,976 | 14,232 | 43,208 | 86,412 |
| Supersedeas bond premium | | | 0 | 5,545 |
| Dues to National (NOLHGA) | 33,091 | | 33,091 | 29,366 |
| Auditing and accounting fees | 4,560 | | 4,560 | 5,663 |
| Bookkeeping fees | 1,995 | | 1,995 | 1,841 |
| Meetings and travel expenses | 1,390 | | 1,390 | 1,000 |
| Subscriptions and publications | 1,007 | | 1,007 | 1,006 |
| Computer services and expenses | 620 | | 620 | 1,184 |
| Teleconferences | 320 | | 320 | 304 |
| Printing, postage, supplies, miscellaneous | 65 | | 65 | 1,340 |
| Refund overpayment of assessments for closed insolvencies | | | 0 | 1,714 |
| Class A general and administration expenses allocated to Classes B and C (Note 9) | (92,571) | 92,571 | 0 | 0 |
| TOTAL EXPENSES | \$ 0 | \$ 539,204 | \$ 539,204 | \$ 572,245 |
| REVENUES OVER EXPENSES | \$ 4,532 | \$ 3,280 | \$ 7,812 | \$1,993,294 |
| Increase in estimated claims payable | | (1,797,748) | (1,797,748) | (95,000) |
| Transfers among net assets (Note 10) | 24,107 | (24,107) | 0 | 0 |
| INCREASE (DECREASE) IN NET ASSETS | \$ 28,639 | \$(1,818,575) | \$(1,789,936) | \$1,898,294 |
| NET ASSETS – BEGINNING OF YEAR | 162,905 | 5,789,866 | 5,952,771 | 4,054,477 |
| NET ASSETS – END OF YEAR | \$ 191,544 | \$ 3,971,291 | \$ 4,162,835 | \$5,952,771 |

See accompanying notes to financial statements.

CLASSES B AND C NET ASSETS – STATEMENTS OF ACTIVITIES

| | Balance 12/31/02 | 1/1 – 12/31/03 Revenues | Expenses | Balance 12/31/03 |
|--|---------------------|----------------------------|-----------|---------------------|
| Class C7 – First Columbia Life, LA | \$ (11,658) | | | |
| Interest expense | | \$ (290) | | \$ (11,948) |
| Class C9 – Amalgamated Labor Life, IL | 96,481 | | | |
| Transferred to Contingency Reserve - Health | | | \$ 96,481 | 0 |
| Class C11 – Knickerbocker Life, TX | 55,871 | | | |
| Investment income | | 1,390 | | 57,261 |
| Class C13 – Life of Indiana | 27,153 | | | |
| Investment income | | 676 | | 27,829 |
| Class C 20 – Executive Life, CA | (5,121,336) | | | |
| Estate distribution | | 1,400 | | |
| Interest expense | | (25,769) | | |
| Assumption reinsurance | | | 387,564 | |
| Assessments by NOLHGA for expenses | | | 27,318 | |
| Administration & legal fees, & direct expenses | | | 10,512 | |
| Allocated general & administration expenses | | | 68,376 | |
| Estimated claims payable decrease | | | (59,000) | (5,580,475) |
| Class C 21 – Mutual Security Life, IN | 5,655,310 | | | |
| Investment income | | 140,688 | | |
| Assessments by NOLHGA for expenses | | | 36 | 5,795,962 |
| Class C 23 – First Capital Life, CA and Fidelity Bankers Life, VA | 25,752 | | | |
| Transferred to Class A – General Administration | | | 25,752 | 0 |
| Class C25 – Midwest Life, LA | 608,718 | | | |
| Investment income | | 15,140 | | |
| Assessments by NOLHGA for expenses | | | 3 | |
| Administration & legal fees, & direct expenses | | | 42 | |
| Allocated general & administration expenses | | | 273 | 623,540 |
| Class C26 – Guaranty Security Life, FL | 1,957,828 | | | |
| Estate distributions | | 226,927 | | |
| Investment income | | 51,909 | | |
| Assessments by NOLHGA for expenses | | | 378 | |
| Administration & legal fees, & direct expenses | | | 60 | |
| Allocated general & administration expenses | | | 390 | 2,235,836 |

(Continued)

CLASSES B AND C NET ASSETS – STATEMENTS OF ACTIVITIES

| | Balance 12/31/02 | <u>1/1 – 12/31/03</u> | | Balance 12/31/03 |
|--|---------------------|-----------------------|-----------------|---------------------|
| | | <u>Revenues</u> | <u>Expenses</u> | |
| Class C27 – Mutual Benefit Life, NJ | \$ 259,981 | | | |
| Estate distribution | | \$ 5,120 | | |
| Investment income | | 6,516 | | |
| Administration & legal fees, & direct expenses | | | \$ 24 | |
| Allocated general & administration expenses | | | 157 | \$ 271,436 |
| Class C28 – United Equitable Life, IL | (39,103) | | | |
| Transferred to Contingency Reserve - Health | | | (39,103) | 0 |
| Class C29 – Inter-American Insurance, IL | 566,698 | | | |
| Estate distribution | | 26,897 | | |
| Investment income | | 14,326 | | |
| Assessments by NOLHGA for expenses | | | 2,594 | |
| Administration & legal fees, & direct expenses | | | 130 | |
| Allocated general & administration expenses | | | 846 | 604,351 |
| Class C30 – Andrew Jackson Life, MS | (1,985) | | | |
| Interest expense | | (49) | | (2,034) |
| Class C31 – Great Republic Life, CA | (2,436) | | | |
| Interest expense | | (61) | | (2,497) |
| Class C32 – Old Faithful Life, WY | 99,143 | | | |
| Investment income | | 2,466 | | 101,609 |
| Class C33 – Old Colony Life, GA | 318,017 | | | |
| Investment income | | 7,912 | | 325,929 |
| Class C34 – New Jersey Life | 54,041 | | | |
| Investment income | | 1,344 | | |
| Assessments by NOLHGA for expenses | | | | 55,385 |
| Class C36 – Pacific Standard Life, CA | 1,132 | | | |
| Investment income | | 11 | | |
| Administration & legal fees, & direct expenses | | | 154 | |
| Allocated general & administration expenses | | | 1,002 | (13) |

(Continued)

CLASSES B AND C NET ASSETS – STATEMENTS OF ACTIVITIES

| | Balance 12/31/02 | 1/1 – 12/31/03 Revenues | Expenses | Balance 12/31/03 |
|--|---------------------|----------------------------|----------|---------------------|
| Class C37 – Kentucky Central Life | \$ 865,717 | | | |
| Investment income | | \$ 21,527 | | |
| Assessments by NOLHGA for expenses | | | \$ 719 | |
| Administration & legal fees, & direct expenses | | | 36 | |
| Allocated general & administration expenses | | | 234 | \$ 886,255 |
| Class C38 – Consumers United, DE | (142,808) | | | |
| Interest expense | | (3,555) | | |
| Assessments by NOLHGA for expenses | | | 136 | (146,499) |
| Class C40 – American Integrity, PA | 876,060 | | | |
| Investment income | | 21,794 | | 897,854 |
| Class C41 – National Heritage, DE | (98,182) | | | |
| Interest expense | | (2,492) | | |
| Assessments by NOLHGA for expenses | | | 751 | |
| Administration & legal fees, & direct expenses | | | 302 | |
| Allocated general & administration expenses | | | 1,964 | (103,691) |
| Class C42 – Summit National Life, PA | 167,730 | | | |
| Investment income | | 4,171 | | |
| Assessments by NOLHGA for expenses | | | 124 | 171,777 |
| Class C43 – Confederation Life, MI | (7,225) | | | |
| Estate distributions | | 937 | | |
| Interest expense | | (173) | | |
| Assessments by NOLHGA for expenses | | | 1 | |
| Administration & legal fees, & direct expenses | | | 52 | |
| Allocated general & administration expenses | | | 338 | (6,852) |
| Class C45 – National American, PA | 144,232 | | | |
| Investment income | | 3,588 | | |
| Assessments by NOLHGA for expenses | | | 34 | 147,786 |
| Class C 49 – First National Life, AL | (1,228) | | | |
| Estate distribution | | 48 | | |
| Interest expense | | (30) | | (1,210) |

(Continued)

CLASSES B AND C NET ASSETS – STATEMENTS OF ACTIVITIES

| | Balance 12/31/02 | 1/1 – 12/31/03 Revenues | Expenses | Balance 12/31/03 |
|---|---------------------|----------------------------|-----------|---------------------|
| Class C60 – First National Life Ins. Co. of America, MS (Thunor) | \$ (307,945) | | | |
| Interest expense | | \$ (7,675) | | |
| Assessments by NOLHGA for expenses | | | \$ 321 | |
| Administration & legal fees, & direct expenses | | | 132 | |
| Allocated general & administration expenses | | | 859 | \$ (316,932) |
| Class C61 – International Financial Services Life, MO (Thunor) | (8,214) | | | |
| Interest expense | | (205) | | (8,419) |
| Class C62 – National Affiliated Investor Life, LA | (16,709) | | | |
| Interest expense | | (422) | | |
| Assessments by NOLHGA for expenses | | | 33 | |
| Administration & legal fees, & direct expenses | | | 54 | |
| Allocated general & administration expenses | | | 352 | (17,570) |
| Class C63 – American Chambers Life, OH | (1,368,799) | | | |
| Interest expense | | (34,068) | | |
| Policyholder benefit claims | | | (2,430) | |
| Assessments by NOLHGA for expenses | | | 2,607 | |
| Administration & legal fees, & direct expenses | | | 272 | |
| Allocated general & administration expenses | | | 1,768 | |
| Estimated claims payable decrease | | | 0 | (1,405,084) |
| Class C64 – Bankers Commercial Life, TX | (43,403) | | | |
| Estate distribution | | 14,053 | | |
| Premiums received | | 3,709 | | |
| Interest expense | | (872) | | |
| Policyholder benefit claims | | | 1,791 | |
| Assessments by NOLHGA for expenses | | | 292 | |
| Administration & legal fees, & direct expenses | | | 364 | |
| Allocated general & administration expenses | | | 2,367 | (31,327) |
| Class C65 – Reliance Insurance Co., PA | (177,705) | | | |
| Interest expense | | (240) | | |
| Policyholder benefit claims | | | 1,479 | |
| Assessments by NOLHGA for expenses | | | (910) | |
| Administration & legal fees, & direct expenses | | | 598 | |
| Allocated general & administration expenses | | | 3,890 | |
| Estimated claims payable decrease | | | (170,000) | (13,002) |

(Continued)

CLASSES B AND C NET ASSETS – STATEMENTS OF ACTIVITIES

| | Balance 12/31/02 | 1/1 – 12/31/03 Revenues | Expenses | Balance 12/31/03 |
|--|---------------------------|----------------------------|---------------------------|---------------------------|
| Class B66 – Legion & Villanova Insurance Cos., PA | \$ (2,798) | | | |
| Interest expense | | \$ (108) | | |
| Administration & legal fees, & direct expenses | | | \$ 334 | |
| Allocated general & administration expenses | | | 2,173 | \$ (5,413) |
| Class B67 – London Pacific Life, NC | (7,483) | | | |
| Interest expense | | (331) | | |
| Assessments by NOLHGA for expenses | | | 8,374 | |
| Administration & legal fees, & direct expenses | | | 640 | |
| Allocated general & administration expenses | | | 4,162 | |
| Estimated claims payable increase | | | 2,026,748 | (2,047,738) |
| Class B Contingency Reserve – Life | 1,100,746 | | | |
| Interest income | | 27,383 | | 1,128,129 |
| Class B Contingency Reserve – Health | 1,221,685 | | | |
| Interest income | | 31,535 | | |
| Transferred from Classes C9 and C28 | | | (57,378) | 1,310,598 |
| TOTAL TEMPORARILY RESTRICTED NET ASSETS | <u>\$5,789,866</u> | <u>\$ 542,484</u> | <u>\$2,361,059</u> | <u>\$3,971,291</u> |
| Per Exhibit B: | | | | |
| Total expenses | | | \$ 539,204 | |
| Transferred to Class A | | | 24,107 | |
| Increase in estimated claims payable | | | 1,797,748 | |
| | | | <u>\$2,361,059</u> | |

STATEMENTS OF CASH FLOWS (Notes 1 and 2)

| | <u>2003</u> | <u>2002</u> |
|---|----------------------------|------------------------------|
| CASH FLOWS FROM (USED FOR) OPERATING ACTIVITIES: | | |
| Increase (decrease) in net assets per Exhibit B | \$(1,789,936) | \$ 1,898,294 |
| Adjustments to reconcile increase in net assets with net cash from operating activities: | | |
| Realized net (gain) loss from sale of investments | 16,024 | (67,248) |
| Unrealized market (gain) loss on investments | 164,516 | (107,955) |
| Decrease in accrued interest receivable | 10,013 | 439 |
| Increase (decrease) in accounts payable | (6,388) | 5,067 |
| Increase in estimated claims payable | <u>1,797,748</u> | <u>95,000</u> |
| NET CASH FROM OPERATING ACTIVITIES | \$ <u>191,977</u> | \$ <u>1,823,597</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from sale of investments | \$ 1,800,000 | \$ 2,768,110 |
| Purchase of investments | <u>(2,294,399)</u> | <u>(5,622,974)</u> |
| NET USED FOR INVESTING ACTIVITIES | \$ <u>(494,399)</u> | \$ <u>(2,854,864)</u> |
| CASH AND MONEY MARKET FUND: | | |
| Decrease during year | \$ (302,422) | \$(1,031,267) |
| Balance at beginning of year | <u>1,119,753</u> | <u>2,151,020</u> |
| Balance at end of year | \$ <u>817,331</u> | \$ <u>1,119,753</u> |
| Balance at end of year | <u>12/31/03</u> | <u>12/31/02</u> |
| Cash in checking account | \$ 151,437 | \$ 244,592 |
| Cash in money market fund | <u>665,894</u> | <u>875,161</u> |
| | \$ <u>817,331</u> | \$ <u>1,119,753</u> |

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION

Nebraska Life and Health Insurance Guaranty Association is a nonprofit, unincorporated association organized and established by the Nebraska Life and Health Insurance Guaranty Act, Sections 44-2701 through 2720, R.S. Supp. 1975, which provides for the creation of an association of member insurers to enable the guaranty of payment of benefits and the continuance of coverage of life insurance policies, health insurance policies, annuity contracts and supplemental contracts. Any insurer licensed to issue life and health insurance policies, and annuity and supplemental contracts in the State of Nebraska is required to be a member.

Association members may be assessed for assessments as follows:

Class A – Assessments for administration expenses of the Association.

Class B – Assessments to cover insurance benefit claims and expenses of domestic (Nebraska) and foreign (other than Nebraska) insurance companies with policyholders in Nebraska that are declared insolvent by the State Department of Insurance.

Effective September 1, 2001, Class C assessments were eliminated by amendment of Nebraska Revised Statute Section 44-2708. Therefore, both domestic and foreign insolvencies are now funded by Class B assessments.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Separate accounts are maintained by type of assessments and by insurers. Interest income and gains or losses on investments are allocated to the respective accounts based on the average quarterly balances of each respective account. Accounts with average positive balances are credited with their allocable share of investment income, and accounts with average negative balances are charged with interest expense on their average deficit balance.

Class A general and administrative expenses are allocated to Class B and Class C insolvencies based on time spent by administrative personnel on the specific insolvencies.

Cash in the checking account and the cash in the money market fund are maintained at high-quality financial institutions. Management believes the Association is not exposed to any significant credit risk on the cash in the checking account and cash in the money market fund.

Investments in debt securities are measured at fair value in the statements of financial position. Unrealized gains or losses are included in the statements of activities. Fair value is based on quoted market prices.

(Continued)

NOTES TO FINANCIAL STATEMENTS

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments that potentially expose the Association to concentrations of credit and market risk consist primarily of investments. The Association's investments do not represent significant concentrations of credit risk. Financial instruments are not held for trading purposes.

The cost of equipment is capitalized and depreciated over five to seven years by the straight-line method.

The Association is a nonprofit, unincorporated entity of the State of Nebraska, and therefore, no income tax returns or return of organization exempt from income tax are required to be filed.

NOTE 3 – U. S. TREASURY NOTES

U. S. Treasury Notes owned as of December 31, 2003, were as follows:

| <u>Date</u> <u>Purchased</u> | <u>Quantity</u> | <u>Purchase</u> <u>Cost</u> | <u>Market</u> <u>Value</u> | <u>Maturity</u> <u>Date</u> | <u>Interest</u> <u>Rate</u> |
|---------------------------------|--------------------|--------------------------------|-------------------------------|--------------------------------|--------------------------------|
| U. S. Treasury Notes: | | | | | |
| 9/05/01 | \$1,000,000 | \$1,047,461 | \$1,073,750 | 11/15/05 | 5.750% |
| 3/19/02 | 1,000,000 | 1,000,156 | 1,060,000 | 5/15/06 | 4.625% |
| 2/04/03 | <u>1,000,000</u> | <u>999,687</u> | <u>1,008,750</u> | 11/15/07 | 3.000% |
| | <u>\$3,000,000</u> | <u>\$3,047,304</u> | <u>\$3,142,500</u> | | |

NOTE 4 – U. S. GOVERNMENT AGENCY BONDS

U. S. Government Agency bonds owned as of December 31, 2003, were as follows:

| <u>Date</u> <u>Purchased</u> | <u>Quantity</u> | <u>Purchase</u> <u>Cost</u> | <u>Market</u> <u>Value</u> | <u>Maturity</u> <u>Date</u> | <u>Interest</u> <u>Rate</u> |
|--|--------------------|--------------------------------|-------------------------------|--------------------------------|--------------------------------|
| Federal Farm Credit Banks: | | | | | |
| 8/28/02 | \$ 500,000 | \$ 499,510 | \$ 504,220 | 10/01/04 | 2.375% |
| 10/02/02 | 250,000 | 272,205 | 266,143 | 9/01/05 | 5.750% |
| Federal Home Loan Banks: | | | | | |
| 9/27/02 | 250,000 | 263,225 | 263,907 | 5/21/07 | 4.650% |
| 10/10/02 | 250,000 | 271,105 | 266,563 | 1/20/06 | 5.370% |
| 10/10/02 | 250,000 | 259,985 | 260,000 | 5/30/06 | 4.015% |
| 9/22/03 | 300,000 | 323,935 | 325,032 | 11/10/08 | 5.385% |
| 11/18/03 | 300,000 | 319,200 | 319,593 | 10/14/08 | 4.925% |
| Federal Home Loan Mortgage Corp.: | | | | | |
| 3/18/02 | 550,000 | 577,088 | 608,608 | 12/13/06 | 6.400% |
| 3/18/02 | 450,000 | 476,892 | 502,312 | 1/05/07 | 6.700% |
| Federal National Mortgage Association: | | | | | |
| 12/15/99 | 1,000,000 | 960,930 | 1,016,560 | 5/14/04 | 5.625% |
| 10/15/02 | <u>500,000</u> | <u>547,290</u> | <u>534,845</u> | 6/10/05 | 6.350% |
| | <u>\$4,600,000</u> | <u>\$4,771,365</u> | <u>\$4,867,783</u> | | |

NOTES TO FINANCIAL STATEMENTS

NOTE 5 – CORPORATE BONDS

Corporate bonds owned as of December 31, 2003, were as follows:

| <u>Date Purchased</u> | <u>Quantity</u> | <u>Purchase Cost</u> | <u>Market Value</u> | <u>Maturity Date</u> | <u>Interest Rate</u> |
|---------------------------------|--------------------|--------------------------|-------------------------|--------------------------|--------------------------|
| Abbot Laboratories Notes: | | | | | |
| 1/17/03 | \$ 300,000 | \$ 334,368 | \$ 328,743 | 3/15/08 | 6.000% |
| Eli Lilly & Co. Global: | | | | | |
| 12/17/02 | 300,000 | 324,389 | 323,388 | 7/15/06 | 5.500% |
| General Electric Capital Corp.: | | | | | |
| 10/11/02 | 300,000 | 312,753 | 319,545 | 6/15/07 | 5.000% |
| Procter & Gamble Co. Notes: | | | | | |
| 4/21/03 | 300,000 | 317,208 | 310,950 | 8/15/08 | 4.300% |
| Wal-Mart Stores, Inc.: | | | | | |
| 10/11/02 | <u>300,000</u> | <u>315,402</u> | <u>310,542</u> | 6/15/05 | 4.150% |
| | <u>\$1,500,000</u> | <u>\$1,604,120</u> | <u>\$1,593,168</u> | | |

NOTE 6 – ESTIMATED CLAIMS PAYABLE AS OF DECEMBER 31, 2003 AND 2002

| <u>Insolvency</u> | <u>12/31/03</u> | <u>12/31/02</u> |
|--|--------------------|--------------------|
| Class C20 – Executive Life, CA | \$4,311,000 | \$4,370,000 |
| Class C65 – Reliance Insurance Co., PA | 0 | 170,000 |
| Class B67 – London Pacific Life, NC | <u>2,026,748</u> | <u>0</u> |
| | <u>\$6,337,748</u> | <u>\$4,540,000</u> |

NOTE 7 – CONTINGENCY RESERVE FOR FUTURE OBLIGATIONS

On April 8, 1999, the Board of Directors approved that net asset balances held for certain settled insolvencies be transferred to a contingency reserve for future Class B obligations of the Nebraska Life and Health Insurance Guaranty Association.

Exhibit B-1 (Page 11) presents an accounting of the Class B contingency reserves for the year 2003. The net asset balances of the contingency reserves were as follows:

| | <u>12/31/03</u> | <u>12/31/02</u> |
|---|--------------------|--------------------|
| Contingency reserve for future obligations – Life | \$1,128,129 | \$1,100,746 |
| Contingency reserve for future obligations – Health | <u>1,310,598</u> | <u>1,221,685</u> |
| | <u>\$2,438,727</u> | <u>\$2,322,431</u> |

NOTES TO FINANCIAL STATEMENTS

| NOTE 8 – INVESTMENT INCOME – NET | <u>2003</u> | <u>2002</u> |
|---|------------------|------------------|
| Interest received on money market funds | \$ 6,190 | \$ 30,705 |
| Interest earned on debt securities | 441,574 | 419,415 |
| Realized net gain (loss) from sale of debt securities | (16,024) | 67,248 |
| Unrealized market gain (loss) | (164,516) | 107,955 |
| Investment management fees | <u>(10,289)</u> | <u>(11,504)</u> |
| | <u>\$256,935</u> | <u>\$613,819</u> |

NOTE 9 – CLASS A GENERAL AND ADMINISTRATIVE EXPENSES ALLOCATED TO
CLASSES B AND C

Class A general and administrative expenses were allocated to Classes B and C insolvencies based on time spent by administrative personnel on the specific insolvencies. This procedure is in accordance with accounting guidelines recommended by the National Organization of Life and Health Insurance Guaranty Associations.

Time spent was determined by the administration and legal fees paid to the Cline, Williams Law Firm, who performs the administration of the Nebraska Life and Health Insurance Guaranty Association. The Cline, Williams Law Firm submits monthly billings for their services for each insolvency.

NOTE 10 – TRANSFERS AMONG NET ASSETS

On April 10, 2003, the Board of Directors authorized the closing and the transfer of account balances for specific insolvencies as of January 1, 2003, as follows:

| | |
|--|-----------------|
| To Contingency Reserve – Health: | |
| Class C 9 – Amalgamated Labor Life, IL | \$96,481 |
| Class C28 – United Equitable Life, IL | <u>(39,103)</u> |
| | <u>\$57,378</u> |
| To Class A – General Administration: | |
| Class C23 – First Capital Life, CA | \$25,752 |
| Class C58 – Settlers Life, VA | <u>(1,645)</u> |
| | <u>\$24,107</u> |